

**BEFORE THE THE STATE OF NEW HAMPSHIRE**

**PUBLIC UTILITIES COMMISSION**

**In the matter of:** )  
**Pennichuck Water Works, Inc.** ) **DW 04-056**  
**Temporary Rate Increase** )

**Direct Prefiled Testimony**

**Of**

**Kenneth E. Traum**  
**Assistant Consumer Advocate**

*Dated: August 19, 2004*

**OFFICE OF CONSUMER ADVOCATE**

**TESTIMONY**

**DW 04-056; Pennichuck Water Works, Inc.**

1   **Q.     Please state your name, business address and position.**

2   A.     My name is Kenneth E. Traum. I am the Assistant Consumer Advocate for the Office of  
3           Consumer Advocate (OCA), which is located at 21 S. Fruit Street, Suite 18, Concord,  
4           New Hampshire 03301. I have been affiliated with the OCA for approximately 15 years.  
5           My resume is included as Attachment 1 herein.

6   **Q.     Please summarize the OCA's position on the Company's request for**  
7           **Temporary rates on this docket?**

8   A.     I believe the Commission has two options:  
9           a.   Deny the Company Temporary Rates based on precedents noted below, or  
10          b.   Grant the Company Temporary Rates at the requested level, and have any  
11               subsequent refund to customers resulting from the true-up with Permanent  
12               Rates include interest at the "consumer cost of money" (i.e. credit card  
13               rates).

14   **Q.     What is the Commission precedent you are referring to?**

15   A.     I have included as Attachments 2 and 3 Orders #20,480 and #20,262. but the  
16           relevant aspect follows:

17               "Pursuant to RSA 378:27, the Commission may set temporary rates for the duration of a  
18               permanent rate proceeding if it determines that the 'public interests requires' In Re:  
19               Hampton Water Works, Inc. the Commission, applying this standard, found that a water

1 utility earning only 160 basis points below its last authorized rate of return had failed to  
2 demonstrate that it was in the public interest to provide for temporary rates where there  
3 was no showing that the ‘underearnings harmed the company’s financial stability or  
4 otherwise disadvantaged the company or its ratepayers.’ Id., at 4.

5 In this case, the Company testified that it was only earning 136 basis points  
6 below its last found rate of return. More importantly, however, the testimony revealed  
7 that the Company does not anticipate any borrowings during the pending case or before  
8 the six month bonding period (See RSA 378:6), that service would not suffer if  
9 temporary rates were not granted and that the Company’s revenue analysis was not  
10 certain as it had not annualized the increased revenues it received in the 1991 in its last  
11 rate case.

12 Thus, the Company has not met its burden of demonstrating that its  
13 ‘underearnings’ harmed the Company’s financial stability or otherwise disadvantaged the  
14 Company or its customers. Nor has the Company demonstrated in some other way that  
15 temporary rates are in the public interest. Therefore, the Company’s request for  
16 temporary rates is denied.”

17  
18 **Q. How far below the last authorized rate of return did the Company claim**  
19 **their test year rate of return was?**

20 A. 231 basis points.

21  
22 **Q. Since 231 is more than the 160 applied in the prior Commission Order, is**  
23 **there an extenuating item the Commission should consider here?**

24 A. Yes. Included in the Pennichuck Annual Report to Shareholders for 2003 which  
25 is public information and filed with the Commission, Mr. Correll the President  
26 and CEO of Pennichuck Corporation made the following statement in his letter to

1 Shareholders:

2 “Annual revenue from our three regulated water utilities was \$18.7 million in  
3 2003, compared to \$18.8 million in 2002, due primarily to the wet summer that  
4 decreased consumption by approximately 10 percent.” (emphasis added)  
5

6 **Q. Have you adjusted or proformed the 2003 results based upon this statement?**

7 A. Yes. Attachment 4 shows the difference in ROI to be 130 basis points or below  
8 the point at which the Commission has previously denied Temporary rates as not  
9 being in the public interest.  
10

11 **Q. You have provided a calculation showing that normalizing test year revenues  
12 and variable costs based on the statement in Mr. Correll’s 2003 letter to  
13 Shareholders increases test year ROI from 6.27% to 7.28%. Applying the  
14 same adjustment to Return on Equity increases the reported 6.12% to what?**

15 A. 8.49% [(\$441,355 + 1,138,000) ÷ \$18,601,000].  
16

17 **Q. Has the Commission recently determined the ROE in any fully litigated  
18 dockets?**

19 A. I am aware of two decisions. In DT 02-110, Order #24,265 dated January 16,  
20 2004 for Verizon New Hampshire the Commission found Verizon’s cost of equity  
21 for retail activities to be 9.82%.

22 And in DT 01-221, Order #24,281 dated February 20, 2004 for Kearsarge  
23 Telephone Company the Commission found the cost of equity to be 8.89%.  
24

1    **Q.    Do you believe the difference in ROE between 8.49% and these recent**  
2    **telephone decisions warrant temporary rates?**

3    A.    No. I believe investors would rely more on Mr. Correll's Letter to Shareholders  
4    which points to higher consumption under more normal conditions.

5  
6    **Q.    Did the Company in its Temporary rate petition or prefiled testimony**  
7    **indicate that if the Commission did not grant temporary rates but made the**  
8    **Company wait to implement an increase pursuant to RSA 378:6 III as an**  
9    **alternative to RSA 378:27, that the Company's ability to provide service and**  
10   **attract financing would be adversely impacted in the interim?**

11   A.    No. Actually in Mr. Correll's direct testimony in the Permanent part of the case  
12   he indicated on page 9 that a significant erosion in Pennichuck's earnings is  
13   coming from the eminent domain process but even that will not cause the  
14   Company a crisis in the near term.

15  
16   **Q.    Does the OCA have an alternative to simply denying Temporary rates which**  
17   **serves the "public interest"?**

18   A.    Yes. What the OCA suggests as an alternative methodology for granting  
19   Temporary rates is very simple. After a utility files for a rate increase and service  
20   is deemed to be acceptable the full increase requested should be put into effect on  
21   a Temporary basis subject to refund and interest.

22   This accomplishes several objectives at once. It eliminates any presumption of  
23   correctness of any rate level, it reduces Commission, Staff, OCA, the utility's and  
24   all other parties cost and time investment in the Temporary rates portion of the

1 docket, and enables the parties to concentrate on the critical, permanent, aspect of  
2 the docket. From the utility's viewpoint it eliminates regulatory lag, as their cash  
3 flow is enhanced after a one month delay.  
4

5 **Q. This methodology appears to protect the utility, what does it do to protect**  
6 **ratepayers?**

7 A. The second part of the proposal which will by its nature self-police the magnitude  
8 of a utility's request, is that any refunds due ratepayers for the difference between  
9 Temporary and Permanent rates should be made with an interest rate  
10 representative of the consumer's cost of money not the utility's. This is not  
11 intended as a penalty. It simply makes ratepayers whole. However, because of  
12 the difference in the cost of money, or discount rates if you prefer, between utility  
13 and ratepayers it "polices" temporary rate requests by simply making ratepayers  
14 "whole", instead of being a private bank for utilities at what are unrealistic rates  
15 from a consumer prospective. In short, it reflects the real economics involved.  
16

17 **Q. What do you mean by the "consumer's cost of money"?**

18 A. When rates are set, today's focus is on the utility's cost of short term debt,  
19 whereas it should be on that and what it costs the average residential customer to  
20 pay higher rates on a Temporary basis. This consumer may have readily available  
21 savings which can be utilized, or on the other end of the spectrum may be living  
22 on the margin where he or she must balance paying bills with putting food on the  
23 table. The "cost of money" to these people may exceed 100%. In the middle of  
24 these two extremes are the customers whose method of making short term loans

1 to a utility is by not paying off their credit card balances. The interest on those  
2 types of cards varies, but one and one-half percent per month is the proxy I have  
3 selected.

4  
5 **Q. Please comment on the issue of rate continuity and signals sent by rate level**  
6 **changes.**

7 A. One of the advantages of our proposal is that because the utility's i.e.,  
8 Pennichuck's earnings might be negatively impacted by imposition of the 18%  
9 interest rate on refunds, they will tailor their initial filing to minimize  
10 vulnerability to balances subject to the 18%. This automatically reduces issues of  
11 rate instability, and is no different than the result if the utility had actually gone  
12 out and borrowed from investors who had an 18% cost of money.

13  
14 **Q. Does this conclude your testimony?**

15 A. Yes.